British Columbia Hydro and Power Authority

2015/16

FIRST QUARTER REPORT

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis (MD&A) reports on British Columbia Hydro and Power Authority's (BC Hydro or the Company) consolidated results and financial position for the three months ended June 30, 2015 and should be read in conjunction with the MD&A presented in the 2015 Annual Report, the 2015 Annual Consolidated Financial Statements of the Company, and the Unaudited Condensed Consolidated Interim Financial Statements and related notes of the Company for the three months ended June 30, 2015.

The Company applies accounting standards as prescribed by the Province of British Columbia ("the Province") which combines the accounting principles of International Financial Reporting Standards (IFRS) with regulatory accounting in accordance with Financial Accounting Standards Board Accounting Standards Codification 980, *Regulated Operations* (ASC 980) (collectively the "Prescribed Standards"). All financial information is expressed in Canadian dollars unless otherwise specified.

This report contains forward-looking statements, including statements regarding the business and anticipated financial performance of the Company. These statements are subject to a number of risks and uncertainties that may cause actual results to differ from those contemplated in the forward-looking statements.

HIGHLIGHTS

- Net income for the three months ended June 30, 2015 was $60 million, $33 million lower than the same period in the prior fiscal year. The decrease from the prior year was primarily due to higher finance charges partially offset by higher domestic revenues.

- Water inflows to the system during the three months ended June 30, 2015 were 101 per cent of average, compared to 99 per cent of average in the same period in the prior fiscal year. The current system inflow for fiscal 2016 is forecast to be 89 per cent of average, compared to the system inflow for fiscal 2015, which was 102 per cent of average.

- Capital expenditures for the three months ended June 30, 2015 were $435 million. BC Hydro continues to invest significantly in capital projects to refurbish its ageing infrastructure and build new assets for future growth, including John Hart Generating Station Replacement, Interior to Lower Mainland Transmission project, Dawson Creek/Chetwynd Area Transmission project, Ruskin Dam Safety and Powerhouse Upgrade project, Site C Clean Energy project and the Upper Columbia Capacity Additions at Mica – Units 5 & 6 project.

($ in millions)	*For the three months ended June 30* **2015**	2014	Change
Net Income	**$ 60**	$ 93	$ (33)
Number of Domestic Customers	**1,940,534**	1,918,776	21,758
GWh Sold (Domestic)	**14,610**	12,049	2,561
Total Reservoir Storage (GWh)	**27,789**	23,726	4,063

($ in millions)	As at June 30, 2015	As at March 31, 2015	Change
Total Assets	**$ 27,964**	$ 27,753	$ 211
Retained Earnings	**$ 4,128**	$ 4,068	$ 60
Debt to Equity	**80 : 20**	80 : 20	N/A

CONSOLIDATED RESULTS OF OPERATIONS

These interim statements present the Company's operating results and financial position under the Prescribed Standards. Under the Prescribed Standards, the Company applies the principles of IFRS plus ASC 980 to reflect the rate-regulated environment in which the Company operates. These principles allow for the deferral of costs and recoveries that under IFRS would otherwise be recorded as expenses or income in the current accounting period. The deferred amounts are either recovered or refunded through future rate adjustments.

The use of regulatory accounts is common amongst regulated utility industries throughout North America. BC Hydro uses various regulatory accounts, in compliance with British Columbia Utilities Commission (BCUC) orders, in order to better match costs and benefits for different generations of customers, smooth out the rate impact of large non-recurring costs, and defer to future periods differences between forecast and actual costs or revenues.

For the three months ended June 30, 2015, transfers resulted in a net decrease to regulatory accounts of $49 million, primarily due to amortization of regulatory accounts and additions to the Finance Charges regulatory liability account due to lower than forecast costs. The decrease was partially offset by additions for the phasing in of the rate impact of the reduction in the amount of overhead eligible for capitalization under IFRS, demand-side management program expenditures (DSM), and increases to the Rate Smoothing regulatory account as part of the 10 year rate plan.

Net income for the three months ended June 30, 2015 was $60 million, $33 million lower than the same period in the prior fiscal year. The decrease from the prior year was primarily due to higher finance charges, partially offset by higher domestic revenues.

REVENUES

Total revenues after regulatory account transfers for the three months ended June 30, 2015 were $1,308 million, a decrease of $62 million or 5 per cent compared to the same period in the prior fiscal year primarily due to lower net electricity trade revenues, partially offset by higher domestic revenues due to higher average customer rates and higher surplus energy sales.

For the three months ended June 30		*(in millions)* 2015	2014	*(gigawatt hours)* 2015	2014	*($ per MWh)*[2] 2015	2014
Domestic							
Residential	$	**392**	$ 376	**3,765**	3,769	**$104.12**	$ 99.76
Light industrial and commercial		**412**	383	**4,485**	4,456	**91.86**	85.95
Large industrial		**184**	181	**3,343**	3,544	**55.04**	51.07
Other energy sales		**137**	68	**3,017**	280	**45.41**	242.86
Total Domestic Revenue Before Regulatory Transfer		**1,125**	1,008	**14,610**	12,049	**77.00**	83.66
Rate smoothing and load variance regulatory transfer		**17**	76	-	-	-	-
Total Domestic	$	**1,142**	$ 1,084	**14,610**	12,049	$ **78.17**	$ 89.97
Trade							
Electricity - Gross	$	**192**	$ 315	**3,840**	7,709	$ **50.00**	$ 40.86
Less: forward electricity purchases		**(65)**	(90)	-	-	-	-
Electricity - Net		**127**	225	-	-	-	-
Gas - Gross		**107**	246	**3,884**	5,341	**27.55**	46.06
Less: forward gas purchases		**(68)**	(185)	-	-	-	-
Gas - Net		**39**	61	-	-	-	-
Total Trade[1]	$	**166**	$ 286	**7,724**	13,050	$ **21.49**	$ 21.92
Total	$	**1,308**	$ 1,370	**22,334**	25,099	$ **58.57**	$ 54.58

[1] *Trade revenue regulatory transfer is netted with the trade cost of energy transfer to reflect a trade margin transfer and this is reflected in the cost of energy table.*
[2] *The Trade $/MWh figures are based on total gross sales which includes physical and financial transactions whereas the volumes only include physical transactions.*

Domestic Revenues

Total domestic revenues after regulatory account transfers for the three months ended June 30, 2015 were $1,142 million, an increase of $58 million or 5 per cent over the same period in the prior fiscal year. Domestic revenues before regulatory account transfers of $1,125 million were $117 million or 12 per cent higher than in the same period in the prior fiscal year. The increase was primarily due to higher other energy sales as a result of surplus energy sold (2,716 GWh) into the market as compared to the same period in the prior fiscal year (10 GWh). Surplus energy sales were required to reduce spill risk as a result of higher reservoir levels resulting from increased storage throughout the fall and winter due to low market prices. In addition, domestic revenues increased due to a 6 per cent rate increase effective April 1, 2015 as approved by the BCUC.

Variances between actual and planned load are deferred to the Non-Heritage Deferral Account (NHDA) and variances between actual and planned other energy sales are deferred to the Heritage Deferral Account (HDA) and NHDA.

Trade Revenues

Powerex, a wholly owned subsidiary of the Company, is a key participant in energy markets across North America, buying and supplying wholesale power, natural gas, ancillary services, financial energy products, and environmental products with an expanding list of trade partners.

The Company's electricity system is interconnected with systems in Alberta and the Western United States, facilitating sales and purchases of electricity outside of British Columbia. Powerex's trade activities help the Company balance its system by being able to import energy to meet domestic demand when there is a supply shortage and exporting energy when there is a supply surplus. Exports are made only after ensuring domestic demand requirements can be met.

Total trade revenues for the three months ended June 30, 2015 were $166 million, a decrease of $120 million or 42 per cent compared with the same period in the prior year. The decrease in revenue was primarily due to a 50 per cent decrease in the volume of physical electricity sold and a 40 per cent decrease

in the average natural gas sales price as well as a 27 per cent decrease in the volume of physical gas sold. The decrease in the volume of physical electricity sold was primarily due to higher volumes of surplus energy sold for domestic purposes. The decrease in the average natural gas sales prices was reflective of an increase in production in the current year as well as overall higher natural gas prices in North America in the prior year due to depleted inventory in storage. The decrease in the volume of physical gas sold was primarily due to lower gas trading opportunities.

Variances between actual and planned trade income (which includes trade revenues) are deferred to the Trade Income Deferral Account (TIDA).

OPERATING EXPENSES

For the three months ended June 30, 2015, total operating expenses of $1,060 million were $77 million lower than in the same period in the prior fiscal year. The decrease was primarily the result of lower electricity and gas purchases partially offset by higher amortization and depreciation and materials and external services costs.

COST OF ENERGY

Energy costs are comprised of electricity and gas purchases for domestic and trade customers, water rentals and transmission and other charges. Energy costs are influenced primarily by the volume of energy consumed by customers, the mix of sources of supply and market prices of energy. The mix of sources of supply is influenced by variables such as the current and forecast market prices of energy, water inflows, reservoir levels, energy demand, and environmental and social impacts.

Total energy costs for the three months ended June 30, 2015 were $459 million, $122 million or 21 per cent lower than the same period in the prior fiscal year. The decrease over the prior fiscal year was primarily due to lower trade electricity and gas purchases.

For the three months ended June 30	*(in millions)* 2015	2014	*(gigawatt hours)* 2015	2014	*($ per MWh)*[2] 2015	2014
Domestic						
Water rental payments (hydro generation)[1]	**$ 80**	$ 85	**12,298**	8,836	**$ 6.68**	$ 9.95
Purchases from Independent Power Producers	**272**	224	**3,735**	3,251	**72.81**	68.82
Other electricity purchases - Domestic	**-**	1	**5**	36	**0.00**	32.89
Gas for thermal generation	**7**	9	**43**	56	**159.37**	162.54
Transmission charges and other expenses	**5**	-	**24**	27	**-**	-
Allocation to/from trade energy	**(6)**	21	**(243)**	631	**24.83**	28.94
Total Domestic Cost of Energy Before Regulatory Transfers	**358**	340	**15,862**	12,837	**22.57**	26.48
Domestic cost of energy regulatory transfers	**(19)**	(2)	**-**	-	**-**	-
Total Domestic	**$ 339**	$ 338	**15,862**	12,837	**$ 21.39**	$ 26.33
Trade						
Electricity - Gross	**$ 93**	$ 192	**3,543**	8,329	**$ 26.25**	$ 23.05
Less: forward electricity purchases	**(65)**	(90)	**-**	-	**-**	-
Electricity - Net	**28**	102	**-**	-	**-**	-
Remarketed gas - Gross	**99**	243	**3,973**	5,455	**24.92**	44.54
Less: forward gas purchases	**(68)**	(185)	**-**	-	**-**	-
Remarketed gas - Net	**31**	58	**-**	-	**-**	-
Transmission charges and other expenses	**51**	72	**-**	-	**-**	-
Allocation to/from domestic energy	**6**	(21)	**243**	(631)	**24.83**	28.94
Total Trade Cost of Energy Before Regulatory Transfers	**116**	211	**7,759**	13,153	**23.29**	22.87
Trade net margin regulatory transfer	**4**	32	**-**	-	**-**	-
Total Trade	**$ 120**	$ 243	**7,759**	13,153	**$ 23.83**	$ 25.34
Total Energy Costs	**$ 459**	$ 581	**23,621**	25,990	**$ 22.17**	$ 25.83

1. Total GWh is net of storage exchange.

2. Total cost per MWh includes other electricity purchases at gross cost.

Domestic Energy Costs

Total domestic energy costs after regulatory account transfers for the three months ended June 30, 2015 were $339 million, consistent with the same period in the prior fiscal year. Domestic energy costs before regulatory account transfers of $358 million for the three months ended June 30, 2015 were $18 million or 5 per cent higher than the same period in the prior fiscal year. The increase was the result of a higher volume of purchases from Independent Power Producers (IPPs) due to an increased number of IPPs in operation, partially offset by higher net trade exports (higher allocation to trade energy).

Water rental payments are based on the prior year's generation and, in the prior fiscal year, less hydro was generated resulting in lower water rental payments in the current year even though hydro generation was 3,462 GWh higher than the prior year. Water rental rates are indexed each calendar year based on the annual percentage change in British Columbia's consumer price index.

Variances between actual and planned domestic cost of energy are transferred to the HDA and NHDA.

Trade Energy Costs

Total trade energy costs after regulatory account transfers for the three months ended June 30, 2015 were $120 million, a decrease of $123 million or 51 per cent compared to the same period in the prior fiscal year. Trade energy costs before regulatory account transfers for the three months ended June 30, 2015 were $116 million, a decrease of $95 million or 45 per cent compared with the same period in the prior year. The decrease was primarily due to a 57 per cent decrease in the volume of physical electricity purchased and a 44 per cent decrease in the average gas purchase price as well as a 27 per cent decrease in the physical

volume of gas purchased. The decrease in volume of physical electricity purchased was consistent with the decrease in physical electricity volumes sold. The decrease in the average gas purchase price was reflective of an increase in production in the current year as well as overall higher natural gas prices in North America in the prior year due to depleted inventory in storage. The decrease in volume of physical gas purchased was consistent with the decrease in physical gas sold.

Variances between actual and planned trade income (which includes trade energy costs) are deferred to the TIDA.

Water Inflows

Water inflows to the system during the three months ended June 30, 2015 were 101 per cent of average, compared to 99 per cent of average in the same period in the prior fiscal year. Observed inflows to Williston and Kinbasket reservoirs were 102 per cent and 125 per cent, respectively. The above average inflows in this period were due in large part to above average temperatures that led to an early snow pack melt. Total inflows into Bridge, Lower Mainland, and Vancouver Island facilities were 86 per cent of average in the current quarter, with record low levels in June due to an extended period of dry weather. The current system inflow for fiscal 2016 is forecast to be 89 per cent of average, compared to the system inflow for fiscal 2015, which was 102 per cent of average.

The Williston and Kinbasket reservoirs have been managed such that system energy storage at the end of June 30, 2015 was 25,600 GWh, or 2,900 GWh above the 10 year historic average. This was 3,900 GWh higher than the system energy storage of 21,700 GWh recorded one year earlier. Williston and Kinbasket reservoir energy contents were 16,700 GWh (1,100 GWh above the 10 year historic average) and 8,900 GWh (1,800 GWh above the 10 year historic average), respectively, with Williston 2,200 GWh higher than the prior fiscal year and Kinbasket 1,700 GWh higher than the prior fiscal year. The above average levels of system storage in the current quarter are a result of above average initial system storage levels at the start of the fiscal year and slightly higher than average inflows during the quarter, offset by net market exports within the quarter.

Personnel Expenses

Personnel expenses include salaries and wages, benefits and post-employment benefits. Personnel expenses for the three months ended June 30, 2015 were $145 million, $8 million higher than the same period in the prior fiscal year, primarily due to higher current service pension costs due to a decline in the discount rate used to calculate pension expense.

Materials and External Services

Expenditures on materials and external services for the three months ended June 30, 2015 were $145 million, $10 million higher than the same period in the prior fiscal year, primarily due to increased expenditures on energy purchase agreements (EPAs) accounted for as finance leases and higher expenditures on maintenance and work programs.

Amortization and Depreciation

Amortization and depreciation expense includes the depreciation of property, plant and equipment (PP&E), intangible assets, and the amortization of certain regulatory assets and liabilities. For the three months ended June 30, 2015, amortization and depreciation expense was $304 million, $14 million or 5 per cent higher than the same period in the prior fiscal year primarily due to an increase in depreciation of property, plant and equipment due to more assets in service.

Grants, Taxes and Other Costs

As a Crown Corporation, the Company is exempt from paying federal and provincial income taxes, but pays local government taxes and grants in lieu to municipalities and regional districts, and school tax to the Province on certain assets. Total grants, taxes and other costs for the three months ended June 30, 2015 were $55 million, comparable to total grants and taxes of $51 million in the same period in the prior fiscal year.

Capitalized Costs

Capitalized costs consist of overhead costs directly attributable to capital expenditures that are transferred from operating costs to PP&E. Certain overhead costs not eligible for capitalization under IFRS are transferred from operating costs to the IFRS PP&E regulatory account. These transfers are amortized over 40 years which approximates the composite average life of the PP&E. In addition, starting fiscal 2013, the ongoing impact of this change is being smoothed into rates over a 10 year period through transfers to the IFRS PP&E regulatory account as approved by the BCUC. As such, each year, $1/10^{th}$ more of ineligible costs will be charged to operating costs such that by the end of year ten, all ineligible costs will be charged to operating costs.

Capitalized costs for the three months ended June 30, 2015 were $48 million, $9 million lower than capitalized costs of $57 million in the same period in the prior fiscal year. The reduction in capitalized costs was primarily due to the annual reduction of the transfer of operating costs to the IFRS PP&E account.

FINANCE CHARGES

Finance charges for the three months ended June 30, 2015 were $188 million, $48 million or 34 per cent higher than the same period in the prior fiscal year. The increase was primarily due to higher planned lease charges, higher planned volume of long-term debt borrowings, and higher planned short term interest rates.

REGULATORY TRANSFERS

The Company has established various regulatory accounts with the approval of the BCUC. Regulatory accounts allow the Company to defer certain types of revenue and cost variances through transfers to and from the accounts which are then included in customer rates in future periods, subject to approval by the BCUC and have the effect of adjusting net income. Net regulatory account transfers are comprised of the following:

(in millions)	*For the three months ended June 30* 2015	2014
Energy Accounts		
Heritage Deferral Account	$ **(83)**	$ (2)
Non-Heritage Deferral Account	**85**	41
Trade Income Deferral Account	**(1)**	(31)
	1	8
Forecast Variance Accounts		
Finance Charges	**(37)**	(5)
Rate Smoothing Account	**27**	38
Other	**(8)**	(10)
	(18)	23
Capital-Like Accounts		
Demand-Side Management (DSM)	**32**	18
Site C	**-**	19
Smart Metering and Infrastructure (SMI)	**3**	3
IFRS Property, Plant and Equipment	**34**	39
	69	79
Non-Cash Accounts		
Environmental Provisions & Costs	**(9)**	6
First Nations Costs & First Nations Provisions	**-**	4
Other	**1**	2
	(8)	12
Amortization of regulatory accounts	**(110)**	(117)
Interest on regulatory accounts	**17**	16
Net change in regulatory accounts	$ **(49)**	$ 21

For the three months ended June 30, 2015, net reductions to the Company's regulatory accounts after amortization were $49 million compared to prior year net additions of $21 million. The net asset balance in the regulatory asset and liability accounts as at June 30, 2015 was an asset of $5,384 million compared to an asset of $5,433 million as at March 31, 2015.

Net reductions to the regulatory accounts during the three months ended June 30, 2015 included:

- Net amortization of $110 million to the regulatory accounts; and
- Transfers of $37 million to the Finance Charges regulatory liability account primarily due to $18 million relating to costs associated with EPAs accounted for as finance leases and $18 million relating to interest rate variance.

These net reductions were partially offset by:

- Transfers to the IFRS PP&E regulatory account for smoothing the rate impact of overhead costs not eligible for capitalization under IFRS as they are not considered directly attributable to the construction of capital assets;
- Planned expenditures on DSM projects, which support energy conservation and;

- Increases to the Rate Smoothing regulatory account for smoothing the rate impacts of the rate increases in the 10 year rate plan;

BC Hydro has regulatory mechanisms in place to collect 24 of 26 regulatory accounts, which represent approximately 89 per cent of the total net regulatory account balance, in rates over various periods.

PAYMENT TO THE PROVINCE

Under a Special Directive from the Province, the Company is required to make an annual payment to the Province (the Payment) on or before June 30 of each year. The Payment is equal to 85 per cent of the Company's net income for the most recently completed fiscal year unless the debt to equity ratio, as defined by the Special Directive, after deducting the Payment, is greater than 80:20. If the Payment would result in a debt to equity ratio exceeding 80:20, then the Payment is the greatest amount that can be paid without causing the debt to equity ratio to exceed 80:20.

No Payment has been accrued as at June 30, 2015 as the Company's debt to equity ratio is at the 80:20 cap prior to the calculation of the Payment. As at March 31, 2015, $264 million was accrued and the Payment to the Province was made in June 2015.

RATE REGULATION

In the process of regulating and setting rates for BC Hydro, the BCUC must ensure that the rates are sufficient to allow BC Hydro to provide reliable electricity service, meet its financial obligations, comply with government policy and achieve an annual rate of return on deemed equity (ROE).

Upcoming Revenue Requirements Application

BC Hydro is undertaking preparations for the filing of its next revenue requirements application planned for February 2016.

Rate Design Application (RDA)

BC Hydro is preparing its next RDA, Module 1 of which is expected to be filed with the BCUC in September 2015, followed by Module 2 within the next 24 months. Among other things, the 2015 RDA will consider and update many of the underlying drivers, analysis and assumptions that impact BC Hydro's rate structures for residential, commercial and industrial customers. Government policy, BC Hydro's load resource balance and energy surplus, conservation results and customer experience with the rate structures will be considered, and may result in amendments or updates to the rate structures. Rate design changes are designed to be revenue neutral to the utility. BC Hydro will also consider the relevant Industrial Electricity Policy Review recommendations, as well as changes to BC Hydro's long run marginal cost which is used in rate design.

Available Transfer Capacity (ATC) Rule

On December 5, 2011, the Alberta Electric System Operator (AESO) filed a proposed rule with the Alberta Utilities Commission (AUC) to allocate ATC between the existing BC - Alberta intertie and new interties when the Alberta system is constrained and cannot accommodate the total ATC of all interties. BC Hydro opposed the proposed rule because of the harm it would cause to the Company and its ratepayers. The AUC issued its decision on February 1, 2013 approving the rule as filed. BC Hydro and Powerex were granted leave to appeal to the Alberta Court of Appeal with the appeal heard on January 15, 2015. On June 3, 2015, the Alberta Court of Appeal dismissed the appeal, concluding that the AUC decision was within the AUC's

area of expertise and therefore not unreasonable. BC Hydro and Powerex do not intend to pursue the matter further.

LIQUIDITY AND CAPITAL RESOURCES

Cash flow provided by operating activities for three months ended June 30, 2015 was $168 million, compared with cash flow provided by operating activities of $138 million in the same period in the prior fiscal year. The increase was primarily due to higher income from operating activities partially offset by changes in working capital.

The long-term debt balance net of sinking funds at June 30, 2015 was $17,290 million, compared with $16,721 million at March 31, 2015. The increase was mainly as a result of an increase in in long-term bond issues totaling $893 million ($900 million par value). These increases were partially offset by a decrease in revolving borrowings of $300 million. Long-term debt increased primarily to fund capital expenditures.

CAPITAL EXPENDITURES

Capital expenditures, which include property, plant and equipment and intangible assets, were as follows:

	For the three months ended June 30	
(in millions)	**2015**	2014
Transmission lines and substation replacements & expansion	**$ 177**	$ 203
Generation replacements and expansion	**110**	103
Distribution system improvements and expansion	**92**	103
General, including technology, vehicles and buildings	**36**	30
Site C Clean Energy project	**20**	-
Total Capital Expenditures	**$ 435**	$ 439

Total capital expenditures presented in this table are different from the expenditures in the Consolidated Interim Statements of Cash Flows due to the effect of accruals related to these expenditures.

Transmission lines and substation capital expenditures includes expenditures on the Interior to Lower Mainland Transmission Line, Dawson Creek/Chetwynd Area Transmission, Surrey Area Substation, and Long Beach Area Reinforcement projects.

Generation capital expenditures include expenditures for John Hart Generating Station Replacement, Ruskin Dam Safety and Powerhouse Upgrade, Upper Columbia Capacity Additions at Mica – Unit 5 and Unit 6, and GM Shrum Units 1-5 Turbine Rehabilitation projects.

Distribution capital expenditures include expenditures on customer driven work, end of life asset replacements, system expansion and improvements, and the Smart Metering and Infrastructure project.

General capital expenditures include expenditures on various technology projects and building development programs.

Site C Clean Energy project expenditures incurred after the provincial government's positive investment decision in December 2014 are recorded as capital and include expenditures in support of construction start scheduled for late July 2015.

RISK MANAGEMENT

BC Hydro is exposed to numerous risks, which can result in safety, environmental, financial, reliability and reputational impacts. The impact of many financial risks associated with uncontrollable external influences on BC Hydro's net income is mitigated through the use of regulatory accounts. Regulatory accounts assist in matching costs and benefits for different generations of customers, to smooth the impact of large, non-recurring costs and to defer for future recovery in rates the differences between planned and actual costs or revenues that arise due to uncontrollable events. BC Hydro has a documented plan for the recovery of its regulatory accounts which it filed with the F15-F16 RRRA.

Significant Financial Risks

The largest sources of variability in BC Hydro's financial performance are typically domestic and trade revenue and cost of energy. Both revenues and cost of energy are influenced by several elements, which generally fall into the following four categories: generation available from BC Hydro-dispatched hydro plants, domestic demand for electricity, energy market prices, and deliveries from EPA contracts.

Neither a high nor a low value of any of these individual drivers is intrinsically positive or negative for BC Hydro's financial results. It is the specific combination of these drivers in any given year which has an impact.

While meeting domestic demand, environmental regulations and treaty obligations, BC Hydro attempts to operate the system to take maximum advantage of market energy prices – buying from the markets when prices are low and selling when prices are high. In doing so, BC Hydro attempts to optimize the combined effects of these elements and reduce the net cost of energy for our customers.

This section should be read in conjunction with the risks disclosed in the Risk Management section in the Management's Discussion and Analysis presented in the Annual Report for the year ended March 31, 2015. In addition, information on risks and opportunities that could significantly impact BC Hydro meeting its objectives are outlined at bchydro.com/serviceplan.

FUTURE OUTLOOK

The *Budget Transparency and Accountability Act* requires that BC Hydro file a Service Plan each year. BC Hydro's Service Plan filed in February 2015 forecasted net income for fiscal 2016 at $653 million.

The Company's earnings can fluctuate significantly due to various non-controllable factors such as the level of water inflows, domestic sales load, market prices for electricity and natural gas, weather temperatures and interest rates. The impact to net income of these non-controllable factors is largely mitigated through the use of regulatory accounts. The Service Plan forecast for fiscal 2016 assumed average water inflows (100 per cent of average), domestic sales of 55,379 GWh, average market energy prices of U.S. $32.22/MWh and short-term interest rates of 1.32 per cent.

BC Hydro filed an updated forecast with the Province in August 2015. The net income forecast for fiscal 2016 remains at $653 million. The significant changes from the Service Plan for fiscal 2016, which has no net income impact after regulatory account transfers, include:

- Domestic tariff sales load of approximately 53,000 GWh, a reduction in domestic tariff sales of 1,320 GWh. Forecast sales in the large industrial, and commercial categories have decreased largely as a result of lower forecast customer load in the mining and pulp & paper sectors due to a delay in start-ups and lower commodity market outlook;

- An increase in forecast surplus sales mainly as a result of a decrease in domestic tariff sales and managing reservoir levels to reduce spill risk;

- An increase in the forecast cost of energy mainly due to higher IPP costs resulting from a change in the accounting treatment of an EPA in fiscal 2015 and higher IPP deliveries. This has been partially offset by lower net market purchases, hydro generation, and non-treaty storage costs; and

- A decrease in short term interest rates to 0.68 per cent.

The impact of the changes above flow through BCUC-approved regulatory accounts and have the effect of putting upward pressure on future rates.

UNAUDITED CONDENSED CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE INCOME

(in millions)	*For the three months ended June 30* 2015	2014
Revenues		
Domestic	$ **1,142**	$ 1,084
Trade	**166**	286
	1,308	1,370
Expenses		
Operating expenses (Note 4)	**1,060**	1,137
Finance charges (Note 5)	**188**	140
Net Income	**60**	93
OTHER COMPREHENSIVE INCOME (LOSS)		
Items Reclassified Subsequently to Net Income		
Effective portion of changes in fair value of derivatives designated as cash flow hedges (Note 15)	**(20)**	(16)
Reclassification to income on derivatives designated as cash flow hedges (Note 15)	**16**	29
Foreign currency translation losses	**(1)**	(5)
Other Comprehensive Income (Loss)	**(5)**	8
Total Comprehensive Income	$ **55**	$ 101

See accompanying Notes to the Unaudited Condensed Consolidated Interim Financial Statements.

UNAUDITED CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION

(in millions)	*As at June 30* 2015	*As at March 31* 2015
ASSETS		
Current Assets		
Cash and cash equivalents	$ 61	$ 39
Accounts receivable and accrued revenue	599	627
Inventories (Note 7)	149	122
Prepaid expenses	220	211
Current portion of derivative financial instrument assets (Note 15)	113	152
	1,142	1,151
Non-Current Assets		
Property, plant and equipment (Note 8)	20,187	19,933
Intangible assets (Note 8)	544	547
Regulatory assets (Note 9)	5,695	5,714
Derivative financial instrument assets (Note 15)	84	97
Other non-current assets (Note 10)	312	311
	26,822	26,602
	$ 27,964	$ 27,753
LIABILITIES AND EQUITY		
Current Liabilities		
Accounts payable and accrued liabilities	$ 1,223	$ 1,708
Current portion of long-term debt (Note 11)	3,398	3,698
Current portion of derivative financial instrument liabilities (Note 15)	77	85
	4,698	5,491
Non-Current Liabilities		
Long-term debt (Note 11)	14,047	13,178
Regulatory liabilities (Note 9)	311	281
Derivative financial instrument liabilities (Note 15)	38	38
Contributions in aid of construction	1,629	1,583
Post-employment benefits (Note 13)	1,506	1,498
Other non-current liabilities (Note 14)	1,510	1,514
	19,041	18,092
Shareholder's Equity		
Contributed surplus	60	60
Retained earnings	4,128	4,068
Accumulated other comprehensive income	37	42
	4,225	4,170
	$ 27,964	$ 27,753

Commitments (Note 8)

See accompanying Notes to the Unaudited Condensed Consolidated Interim Financial Statements.

Approved on behalf of the Board:

Stephen Bellringer
Chair, Board of Directors

James Brown
Chair, Audit & Finance Committee

UNAUDITED CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY

(in millions)	Cumulative Translation Reserve	Unrealized Gains/(Losses) on Cash Flow Hedges	Total Accumulated Other Comprehensive Income	Contributed Surplus	Retained Earnings	Total
Balance, April 1, 2014	$ 33	$ 21	$ 54	$ 60	$ 3,751	$ 3,865
Comprehensive Income (Loss)	(5)	13	8	-	93	101
Balance, June 30, 2014	$ 28	$ 34	$ 62	$ 60	$ 3,844	$ 3,966
Balance, April 1, 2015	$ 67	$ (25)	$ 42	$ 60	$ 4,068	$ 4,170
Comprehensive Income (Loss)	(1)	(4)	(5)	-	60	55
Balance, June 30, 2015	$ 66	$ (29)	$ 37	$ 60	$ 4,128	$ 4,225

See accompanying Notes to the Unaudited Condensed Consolidated Interim Financial Statements.

UNAUDITED CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS

(in millions)	*For the three months ended June 30* 2015	2014
Operating Activities		
Net income	$ **60**	$ 93
Regulatory account transfers (Note 9)	**(61)**	(138)
Adjustments for non-cash items:		
Amortization of regulatory accounts (Note 9)	**110**	117
Amortization and depreciation expense (Note 6)	**186**	167
Interest accrual	**171**	162
Other items	**63**	29
	529	430
Changes in:		
Accounts receivable and accrued revenue	**27**	147
Prepaid expenses	**(11)**	(18)
Inventories	**(26)**	(53)
Accounts payable, accrued liabilities and other non-current liabilities	**(135)**	(149)
Contributions in aid of construction	**47**	27
	(98)	(46)
Interest paid	**(263)**	(246)
Cash provided by operating activities	**168**	138
Investing Activities		
Property, plant and equipment and intangible asset expenditures	**(471)**	(432)
Cash used in investing activities	**(471)**	(432)
Financing Activities		
Long-term debt:		
Issued (Note 11)	**893**	694
Retired	**-**	(325)
Receipt of revolving borrowings	**1,717**	2,036
Repayment of revolving borrowings	**(2,016)**	(2,042)
Payment to the Province (Note 12)	**(264)**	(167)
Other items	**(5)**	(4)
Cash provided by financing activities	**325**	192
Increase (decrease) in cash and cash equivalents	**22**	(102)
Cash and cash equivalents, beginning of period	**39**	107
Cash and cash equivalents, end of period	$ **61**	$ 5

See accompanying Notes to the Unaudited Condensed Consolidated Interim Financial Statements.

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS FOR THE THREE MONTHS ENDED JUNE 30, 2015

NOTE 1: REPORTING ENTITY

British Columbia Hydro and Power Authority (BC Hydro) was established in 1962 as a Crown corporation of the Province of British Columbia (the Province) by enactment of the *Hydro and Power Authority Act*. As directed by the *Hydro and Power Authority Act*, BC Hydro's mandate is to generate, manufacture, conserve and supply power. BC Hydro owns and operates electric generation, transmission and distribution facilities in the province of British Columbia.

The condensed consolidated interim financial statements of BC Hydro include the accounts of BC Hydro and its principal wholly owned operating subsidiaries Powerex Corp. (Powerex), Powertech Labs Inc. (Powertech), and Columbia Hydro Constructors Ltd. (Columbia), (collectively with BC Hydro, "the Company") including BC Hydro's one third interest in the Waneta Dam and Generating Facility (Waneta). All intercompany transactions and balances are eliminated upon consolidation.

The Company accounts for its one third interest in Waneta as a joint operation. The consolidated financial statements include the Company's proportionate share in Waneta, including its share of any liabilities and expenses incurred jointly with Teck Metals Ltd. and its revenue from the sale of the output in relation to Waneta.

NOTE 2: BASIS OF PRESENTATION

Basis of Accounting

These condensed consolidated interim financial statements have been prepared in accordance with significant accounting policies that have been established based on the financial reporting provisions prescribed by the Province pursuant to Section 23.1 of the *Budget Transparency and Accountability Act* (BTAA) and Section 9.1 of the *Financial Administration Act* (FAA). In accordance with the directive issued by the Province's Treasury Board, BC Hydro is to prepare its consolidated financial statements in accordance with the accounting principles of International Financial Reporting Standards (IFRS), combined with regulatory accounting in accordance with Financial Accounting Standards Board Accounting Standards Codification 980 (ASC 980), *Regulated Operations* (collectively the "Prescribed Standards"). The application of ASC 980 results in BC Hydro recognizing in the statement of financial position the deferral and amortization of certain costs and recoveries that have been approved by the British Columbia Utilities Commission (BCUC) for inclusion in future customer rates. Such regulatory costs and recoveries would be included in the determination of comprehensive income unless recovered in rates in the periods the amounts are incurred.

The impact of the application of ASC 980 on these condensed consolidated interim financial statements with respect to BC Hydro's regulatory accounts is described in Note 9.

These condensed consolidated interim statements have been prepared by management in accordance with the principles of IAS 34, *Interim Financial Reporting* and the Prescribed Standards and were prepared using the same accounting policies as described in BC Hydro's 2015 Annual Report except as described in Note 3. These interim condensed consolidated financial statements should be read in conjunction with the Annual Consolidated Financial Statements and accompanying notes in BC Hydro's 2015 Annual Report. Certain amounts in the prior year's comparative figures have been reclassified to conform to the current year's presentation.

These condensed consolidated interim financial statements were approved on behalf of the Board of Directors on August 13, 2015.

NOTE 3: CHANGES IN ACCOUNTING POLICIES

Effective April 1, 2015, the Company adopted Amendments to IAS 19, *Employee Benefits* which had no impact on the consolidated financial statements.

NOTE 4: OPERATING EXPENSES

	For the three months ended June 30	
(in millions)	**2015**	2014
Electricity and gas purchases	**$ 334**	$ 457
Water rentals	**91**	89
Transmission charges	**34**	35
Personnel expenses	**145**	137
Materials and external services	**145**	135
Amortization and depreciation (Note 6)	**304**	290
Grants, taxes and other costs	**55**	51
Capitalized costs	**(48)**	(57)
	$ 1,060	$ 1,137

NOTE 5: FINANCE CHARGES

	For the three months ended June 30	
(in millions)	**2015**	2014
Interest on long-term debt	**$ 193**	$ 166
Interest on finance lease liabilities	**23**	6
Net interest expense on net defined benefit liability	**-**	1
Less: capitalized interest	**(15)**	(17)
Total finance costs	**201**	156
Other recoveries	**(13)**	(16)
	$ 188	$ 140

NOTE 6: AMORTIZATION AND DEPRECIATION

(in millions)	*For the three months ended June 30* **2015**	2014
Depreciation of property, plant and equipment	**$ 170**	$ 151
Amortization of intangible assets	**16**	16
Amortization of regulatory accounts	**118**	123
	$ 304	$ 290

NOTE 7: INVENTORIES

(in millions)	*As at June 30* **2015**	*As at March 31* 2015
Materials and supplies	**$ 115**	$ 110
Natural gas trading inventories	**34**	12
	$ 149	$ 122

No natural gas trading inventories are pledged as security for liabilities.

NOTE 8: PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

Property, plant and equipment and intangible asset expenditures for the three months ended June 30, 2015 were $435 million (2014 – $439 million).

As of June 30, 2015, the Company has contractual commitments to spend $1,526 million on major property, plant and equipment projects (for individual projects greater than $50 million).

NOTE 9: RATE REGULATION

Regulatory Accounts

The following regulatory assets and liabilities have been established through rate regulation. In the absence of rate regulation, these amounts would be reflected in comprehensive income unless the Company sought recovery through rates in the period which they are incurred. For the three month period ended June 30, 2015, the impact of regulatory accounting has resulted in a net decrease of $49 million to comprehensive income (June 30, 2014 - $21 million increase). For each regulatory account, the amount reflected in the Net Change column in the following regulatory table represents the impact on comprehensive income for the applicable period, unless otherwise recovered through rates. Under rate regulated accounting, a net decrease in a regulatory asset or a net increase in a regulatory liability results in a decrease to comprehensive income.

(in millions)	*April 1 2015*	*Addition (Reduction)*	*Interest*	*Amortization*	*Net Change*	*June 30 2015*
Regulatory Assets						
Heritage Deferral Account	$ 165	$ (83)	$ 1	$ (9)	$ (91)	$ 74
Non-Heritage Deferral Account	524	85	5	(27)	63	587
Trade Income Deferral Account	244	(1)	2	(12)	(11)	233
Demand-Side Management Programs	842	32	-	(20)	12	854
First Nations Costs & First Nations Provisions	564	-	2	(11)	(9)	555
Non-Current Pension Cost	564	-	-	(4)	(4)	560
Site C	419	-	4	-	4	423
CIA Amortization	87	1	-	-	1	88
Environmental Provisions & Costs	382	(9)	-	(17)	(26)	356
Smart Metering and Infrastructure (SMI)	283	3	3	(8)	(2)	281
IFRS Pension & Other Post-Employment Benefits	650	-	-	(10)	(10)	640
IFRS Property, Plant and Equipment	758	34	-	(5)	29	787
Rate Smoothing Account	166	27	-	-	27	193
Other Regulatory Accounts	66	2	-	(4)	(2)	64
Total Regulatory Assets	5,714	91	17	(127)	(19)	5,695
Regulatory Liabilities						
Future Removal and Site Restoration Costs	33	-	-	(8)	(8)	25
Foreign Exchange Gains and Losses	71	2	-	-	2	73
Finance Charges	173	37	-	(6)	31	204
Other Regulatory Accounts	4	8	-	(3)	5	9
Total Regulatory Liabilities	281	47	-	(17)	30	311
Net Regulatory Asset	$ 5,433	$ 44	$ 17	$ (110)	$ (49)	$ 5,384

NOTE 10: OTHER NON-CURRENT ASSETS

(in millions)	***As at June 30* 2015**	*As at March 31* 2015
Sinking funds	**$ 155**	$ 155
Non-current receivable	**157**	156
	$ 312	$ 311

NOTE 11: LONG-TERM DEBT AND DEBT MANAGEMENT

The Company's long-term debt comprises bonds and revolving borrowings obtained under an agreement with the Province.

In the three month period ended June 30, 2015, the Company issued bonds with net proceeds of $893 million and par value of $900 million (2014 - net proceeds of $694 million and par value of $765 million), a weighted average effective interest rate of 2.8 per cent (2014 - 3.7 per cent) and a weighted average term to maturity of 25.4 years (2014 – 30.1 years).

NOTE 12: CAPITAL MANAGEMENT

Orders in Council from the Province establish the basis for determining the Company's equity for regulatory purposes, as well as the annual Payment to the Province (see below). Capital requirements are consequently managed through the retention of equity subsequent to the Payment to the Province and a limit on the Payment to the Province if it would cause the debt to equity ratio to exceed 80:20.

The Company monitors its capital structure on the basis of its debt to equity ratio. For this purpose, the applicable Order in Council defines debt as revolving borrowings and interest-bearing borrowings less investments held in sinking funds and cash and cash equivalents. Equity comprises retained earnings, accumulated other comprehensive income and contributed surplus.

During the three months ended June 30, 2015, there were no changes in the approach to capital management.

The debt to equity ratio at June 30, 2015, and March 31, 2015 was as follows:

(in millions)	***As at June 30 2015***	*As at March 31 2015*
Total debt, net of sinking funds	**$ 17,290**	$ 16,721
Less: Cash and cash equivalents	**(61)**	(39)
Net Debt	**$ 17,229**	$ 16,682
Retained earnings	**$ 4,128**	$ 4,068
Contributed surplus	**60**	60
Accumulated other comprehensive income	**37**	42
Total Equity	**$ 4,225**	$ 4,170
Net Debt to Equity Ratio	**80 : 20**	80 : 20

Payment to the Province

The Company is required to make an annual Payment to the Province (the Payment) on or before June 30 of each year. The Payment is equal to 85 per cent of the Company's net income for the most recently completed fiscal year unless the debt to equity ratio, as defined by the Province, after deducting the Payment, is greater than 80:20. If the Payment would result in a debt to equity ratio exceeding 80:20, then

the Payment is the greatest amount that can be paid without causing the debt to equity ratio to exceed 80:20.

No Payment has been accrued as at June 30, 2015 as the Company's debt to equity ratio is at the 80:20 cap prior to the calculation of the Payment. As at March 31, 2015, $264 million was accrued (included in accounts payable and accrued liabilities) and the Payment to the Province was made in June 2015.

NOTE 13: POST-EMPLOYMENT BENEFITS

The expense recognized in the statement of comprehensive income for the Company's defined benefit plans prior to any capitalization of employment costs attributable to property, plant and equipment and intangible asset additions and prior to the application of regulatory accounting for the three months ended June 30, 2015 was $43 million (2014 - $36 million).

Company contributions to the registered defined benefit pension plans for the three months ended June 30, 2015 were $16 million (2014 - $16 million).

NOTE 14: OTHER NON-CURRENT LIABILITIES

(in millions)	*As at June 30* **2015**	*As at March 31* 2015
Provisions		
Environmental liabilities	**$ 354**	$ 368
Decommissioning obligations	**52**	53
Other	**24**	27
	430	448
First Nations liabilities	**401**	414
Finance lease obligations	**254**	259
Other liabilities	**97**	81
Deferred revenue - Skagit River Agreement	**447**	441
	1,629	1,643
Less: Current portion, included in accounts payable and accrued liabilities	**(119)**	(129)
	$ 1,510	$ 1,514

NOTE 15: FINANCIAL INSTRUMENTS

Finance charges, including interest income and expenses, for financial instruments disclosed in this note are prior to the application of regulatory accounting for the three months ended June 30, 2015 and 2014.

Categories of Financial Instruments

The following table provides a comparison of carrying values and fair values for non-derivative financial instruments as at June 30, 2015 and March 31, 2015. The non-derivative financial instruments, where

carrying value differs from fair value, would be classified as Level 2 of the fair value hierarchy.

(in millions)	June 30 2015 Carrying Value	June 30 2015 Fair Value	March 31, 2015 Carrying Value	March 31, 2015 Fair Value
Financial Assets and Liabilities at Fair Value Through Profit or Loss:				
Cash equivalents	**$ 48**	**$ 48**	$ 11	$ 11
Loans and Receivables:				
Accounts receivable and accrued revenue	**599**	**599**	627	627
Non-current receivable	**157**	**154**	156	162
Cash	**13**	**13**	28	28
Held to Maturity:				
Sinking funds – US	**155**	**173**	155	184
Other Financial Liabilities:				
Accounts payable and accrued liabilities	**(1,223)**	**(1,223)**	(1,708)	(1,708)
Revolving borrowings - CAD	**(2,045)**	**(2,045)**	(2,623)	(2,623)
Revolving borrowings - US	**(1,202)**	**(1,202)**	(924)	(924)
Long-term debt (including current portion due in one year)	**(14,198)**	**(16,702)**	(13,329)	(16,799)
First Nations liabilities (non-current portion)	**(376)**	**(593)**	(391)	(758)
Finance lease obligations (non-current portion)	**(235)**	**(235)**	(240)	(240)
Other liabilities	**(97)**	**(100)**	(81)	(86)

The carrying value of cash equivalents, loans and receivables, and accounts payable and accrued liabilities approximates fair value due to the short duration of these financial instruments.

The fair value of derivative instruments designated and not designated as hedges, was as follows:

(in millions)	June 30, 2015 Fair Value	March 31, 2015 Fair Value
Derivative Instruments Used to Hedge Risk Associated with Long-term Debt:		
Foreign currency contracts (cash flow hedges for $US denominated long-term debt)	**$ 25**	$ 45
Non-Designated Derivative Instruments:		
Foreign currency contracts	**11**	31
Commodity derivatives	**46**	50
	57	81
Net asset	**$ 82**	$ 126

The carrying value of derivative instruments designated and not designated as hedges was the same as the fair value.

The derivatives are represented on the statement of financial position as follows:

(in millions)	June 30 2015	March 31 2015
Current portion of derivative financial instrument assets	$ 113	$ 152
Current portion of derivative financial instrument liabilities	(77)	(85)
Derivative financial instrument assets, non-current	84	97
Derivative financial instrument liabilities, non-current	(38)	(38)
Net asset	$ 82	$ 126

For designated cash flow hedges for the three months ended June 30, 2015, a loss of $20 million (2014 - $16 million loss) was recognized in other comprehensive income. For the three months ended June 30, 2015, $16 million (2014 - $29 million) was removed from other comprehensive income and reported in net income, offsetting foreign exchange gains (2014 – gains) recorded in the period.

For derivative instruments not designated as hedges, $nil (2014 - $3 million loss) was recognized in finance charges for the three months ended June 30, 2015 with respect to foreign currency contracts for cash management purposes. For the three months ended June 30, 2015, a loss of $14 million (2014 - $7 million loss) was recognized in finance charges with respect to foreign currency contracts for U.S. short-term borrowings. These economic hedges offset $13 million of foreign exchange revaluation gains (2014 - $7 million gain) recorded with respect to U.S. short-term borrowings for the three months ended June 30, 2015. A net loss of $4 million (2014 - $15 million gain) was recorded in trade revenue for the three months ended June 30, 2015 with respect to commodity derivatives.

Inception Gains and Losses

Changes in deferred inception gains and losses arising from the determination of fair value of derivative financial instruments which are not supported by observable current market transactions or valuation models using only observable market data are as follows:

(in millions)	*For the three months ended June 30* 2015	2014
Deferred inception loss, beginning of the period	$ 70	$ 50
New transactions	(1)	(3)
Amortization	(7)	1
Deferred inception loss, end of the period	$ 62	$ 48

Fair Value Hierarchy

The following provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped based on the lowest level of input that is significant to that fair value measurement.

The inputs used in determining fair value are characterized by using a hierarchy that prioritizes inputs based on the degree to which they are observable. The three levels of the fair value hierarchy are as follows:

- Level 1 - values are quoted prices (unadjusted) in active markets for identical assets and liabilities.
- Level 2 - inputs are those other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, as of the reporting date.
- Level 3 - inputs are those that are not based on observable market data.

The following table presents the financial assets and financial liabilities measured at fair value for each hierarchy level as at June 30, 2015 and March 31, 2015:

As at June 30, 2015 *(in millions)*	Level 1	Level 2	Level 3	Total
Short-term investments	$ 48	$ -	$ -	$ 48
Derivatives designated as hedges	-	43	-	43
Derivatives not designated as hedges	53	67	34	154
Total financial assets carried at fair value	$ 101	$ 110	$ 34	$ 245
Derivatives designated as hedges	$ -	$ (18)	$ -	$ (18)
Derivatives not designated as hedges	(48)	(46)	(3)	(97)
Total financial liabilities carried at fair value	$ (48)	$ (64)	$ (3)	$ (115)

As at March 31, 2015 *(in millions)*	Level 1	Level 2	Level 3	Total
Short-term investments	$ 11	$ -	$ -	$ 11
Derivatives designated as hedges	-	53	-	53
Derivatives not designated as hedges	72	77	47	196
Total financial assets carried at fair value	$ 83	$ 130	$ 47	$ 260
Derivatives designated as hedges	$ -	$ (8)	$ -	$ (8)
Derivatives not designated as hedges	(76)	(31)	(8)	(115)
Total financial liabilities carried at fair value	$ (76)	$ (39)	$ (8)	$ (123)

The Company determines Level 2 fair values for debt securities and derivatives using discounted cash flow techniques, which uses contractual cash flows and market-related discount rates.

Level 2 fair values for energy derivatives are determined using inputs other than unadjusted quoted prices that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). Level 2 includes bilateral and over-the-counter contracts valued using interpolation from observable forward curves or broker quotes from active markets for similar instruments and other publicly available data, and options valued using industry-standard and accepted models incorporating only observable data inputs.

There were no transfers between Levels 1 and 2 during the period.

Powerex holds congestion products and structured power transactions that require the use of unobservable inputs when observable inputs are unavailable. Congestion products are valued using forward spreads at liquid hubs that include adjustments for the value of energy at different locations relative to the liquid hub as well as other adjustments that may impact the valuation. Option pricing models are used when the congestion product is an option. Structured power transactions are valued using standard contracts at a

liquid hub with adjustments to account for the quality of the energy, the receipt or delivery location, and delivery flexibility where appropriate. Significant unobservable inputs include adjustments for the quality of the energy and the transaction location relative to the reference standard liquid hub.

The following table reconciles the changes in the balance of financial instruments carried at fair value on the statement of financial position, classified as Level 3, for the three months ended June 30, 2015 and 2014:

(in millions)		
Balance at April 1, 2015	**$**	**39**
Cumulative impact of net loss recognized		(12)
New transactions		(1)
Existing transactions settled		5
Balance at June 30, 2015	**$**	**31**

(in millions)		
Balance at April 1, 2014	**$**	**43**
Cumulative impact of net gain recognized		18
New transactions		(6)
Existing transactions settled		(31)
Balance at June 30, 2014	**$**	**24**

Level 3 fair values for energy derivatives are determined using inputs that are not observable. Level 3 includes instruments valued using observable prices adjusted for unobservable basis differentials such as delivery location and product quality, instruments which are valued by extrapolation of observable market information into periods for which observable market information is not yet available, and instruments valued using internally developed or non-standard valuation models.

A net loss of $7 million (2014 – net gain of $10 million) recognized in net income during the three months ended June 30, 2015 relates to Level 3 financial instruments held at June 30, 2015. The net loss is recognized in trade revenue.

Methodologies and procedures regarding Powerex's energy trading Level 3 fair value measurements are determined by the Powerex's Risk Management group. Level 3 Powerex fair values are calculated within the Powerex's Risk Management Policy for trading activities based on underlying contractual data as well as observable and non-observable inputs. Development of non-observable inputs requires the use of judgment. To ensure reasonability, Level 3 fair value measurements are reviewed and validated by Powerex's Risk Management and Finance departments on a regular basis.

NOTE 16: SEASONALITY OF OPERATING RESULTS

Due to the seasonal nature of the Company's operations, the condensed consolidated interim statement of comprehensive income is not indicative of operations on an annual basis. Seasonal impacts of weather, including its impact on water inflows, energy consumption within the region and market prices of energy, can have a significant impact on the Company's operating results.